Statement of

David G. Kittle, CMB

Chairman-Elect, Mortgage Bankers Association

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"Growing Mortgage Foreclosure Crisis: Identifying Solutions and Dispelling Myths"

Madam Chairwoman, Ranking Member Cannon and members of the Committee, I am David G. Kittle, CMB, President and Chief Executive Officer of Principle Wholesale Lending, Inc. in Louisville, Kentucky and Chairman-Elect of the Mortgage Bankers Association (MBA).[1] I appreciate the opportunity to appear before you today to testify on behalf of MBA and the mortgage industry concerning the situation in today's market, to help identify solutions and to dispel the myths about legislation that would alter the treatment of home mortgages under Chapter 13 of the Bankruptcy Code.

The myths most in need of dispelling concern H.R. 3609, the ''Emergency Home Ownership and Mortgage Equity Protection Act of 2007,'' introduced by Representative Brad Miller and Chairwoman Linda Sanchez and amended by Representative Steve Chabot in the full Judiciary Committee. The amended bill makes key changes to Chapter 13 of the Bankruptcy Code including allowing the following changes for seven years:

- modification of "subprime" and "non-traditional" mortgages secured by principal residences ("home mortgages") originated between 2000 and the date of enactment of the bill;

- allowing home loans to be repaid beyond the term of the Chapter 13 plan, which today cannot exceed three to five years;

- eliminating the requirement to obtain credit counseling before the debtor can file for bankruptcy when the lender has notified the debtor that it may foreclose the loan; and

- requiring that fees and charges, accruing during the bankruptcy proceeding be filed with the court and that such fees do not exceed the value of the property.

If these provisions are enacted, there will be significant consequences for future borrowers, mortgage servicers, investors, pension funds and other global investors in mortgage-backed securities (MBS), as well as, the entire American economy. For these and other reasons, MBA opposes H.R. 3609.

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 500,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 3,000 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

Myth: H.R. 3609 Simply Closes a Loophole in the Bankruptcy Code
Fact: Congress Deliberately Acted to Improve Mortgage Market Liquidity

Today, a mortgage secured by the principal residence of a debtor cannot be modified in bankruptcy. This policy has been in existence over 100 years, since the Bankruptcy Act of 1898, and is a cornerstone to an efficient U.S. residential mortgage market. The protection provided to home mortgages was not a loophole or oversight. It was a deliberate act of Congress to ensure the continued low cost and free flow of home mortgage credit (see Legislative History, Attachment A). A shift in public policy to remove such protections will encourage debtors not to pay their contractual mortgage obligations and would dramatically change the residential mortgage market. H.R. 3609 would introduce significant risks for home lenders, investors and loan servicers. The risks include the ability to set aside certain mortgage contracts and modify interest rates and other terms. It would also allow liens to be stripped down to the fair market value of the underlying properties, although the bill does not define fair market value. The increased risk would result in mortgage lenders passing on the associated costs to borrowers in the form of higher interest rates and fees.

Myth: Passing H.R. 3609 (Chabot Compromise) Will Have Little Impact on Servicers and the Mortgage Market
Fact: H.R. 3609 Will Have Immediate and Long-Term Impact on the Mortgage Market

If H.R. 3609 were enacted, lenders, securitizers, investors, and loan servicers would see significant new risks on their existing portfolios. Because the bill, as amended by the Chabot Compromise, continues to be retroactive, these parties would absorb significant immediate losses that could have dire financial consequences. The obvious outcome of the bill would be that large principal losses never anticipated or priced into the interest rate or closing costs when the loan was made would have to be absorbed. Bondholders, including mutual funds, pension funds and government entities would see their investments decline. Servicers who never assumed principal risk of loss would suddenly have to absorb losses due to the loss of credit enhancements. Servicers and portfolio lenders with origination capability could offset the losses with new lending, however, such loans would have to carry higher interest rates and costs. Given the decline in originations, the costs would have to be concentrated on a smaller population and thus the cost of credit would be higher per borrower than if applied across a larger home buying or refinance population. The correlation of losses to income is not perfect and, as a result, new loan costs would be higher than necessary to cover real and anticipated losses and to ensure mortgage companies' continued solvency.

Moreover, bankruptcy attorneys would aggressively advertise to borrowers to seek the benefits of this bill if their homes have declined in value, whether or not the borrower is in default. The cost of defending these bankruptcy cases would be staggering to the industry.

We believe that it is important for Congress to understand what H.R. 3609 actually does, to understand why it would so drastically affect the mortgage market and why MBA opposes its passage. In addition to the risks previously described, other risks are introduced, perhaps unintended, but which would have serious consequences. We would like to discuss the full range of risks in greater detail, which will illustrate why MBA is so concerned with this bill.

Myth: H.R. 3609 Would Not Have a Negative Effect on Mortgage Market Participants
Fact: Key Provisions of H.R. 3609 Would Introduce Substantial New Risks and Losses for Mortgage Market Participants

A. Permits Modifications and Strip Downs of Home Mortgages

As stated above, the bill amends section 1322(b)(2) of the Bankruptcy Code, which currently prohibits bankruptcy judges from modifying the terms of mortgages secured by “principal residences” in Chapter 13. The bill would permit bankruptcy courts to change the terms of certain mortgages without the lender’s consent (often referred to as a “cram down”), including modifying the interest rate, extending the maturity date, capitalizing arrearages and reamortizing the loan. In addition, judges would be granted the authority to “strip down” a secured home mortgage. A strip down (sometimes also known as a “lien strip”) is a type of cram down that effectively converts the portion of the secured debt that exceeds the fair market value of the home into unsecured debt. The unsecured portion is treated like other unsecured debt, which is generally paid little or nothing through the Chapter 13 Plan, and is discharged upon successful completion of the plan.

The modification provisions in H.R. 3609 apply to the vast majority of “subprime” and all “non-traditional” mortgages secured by principal residences.” Unfortunately, the definition of “subprime” would also cover a significant number of prime loans. Needless to say, this broad application of cram downs to these mortgages would introduce substantial new risks not priced into the product or contemplated when originally setting servicing fees.

B. H.R. 3609 Eliminates Substantial Controls

In addition to permitting cram downs of home mortgages, H.R. 3609 goes further and would remove significant controls that virtually ensure that bankruptcy filings will skyrocket. Consumer groups perpetuate the myth the bill will *not* substantially increase creditor risk or mortgage costs because there are few cram downs of second homes and investor properties since cram downs were permitted on those property types in 1978. Consumer groups fail to mention the whole truth.

H.R. 3609 would create a quintessential moral hazard. Today, the Bankruptcy Code generally allows mortgages other than those secured by principal residences of the debtor to be crammed down. However, if such loans are crammed down, the debtor must pay the *entire amount* of the secured claim within the three-to-five-year duration of the Chapter 13 plan.[2] The unsecured portion of the claim that gets crammed down gets an apportioned payment to the extent there is additional income or cash that can support those payments. If there are no funds remaining to pay unsecured creditors after paying secured and priority claims, the unsecured creditors receive nothing and the unsecured debt is discharged upon termination of the plan. For example, under current law, if a mortgage contract of $150,000 gets stripped down to $100,000, the debtor must pay the entire $100,000 within three-to-five years in equal monthly installments. This control limits unbridled runs on the bankruptcy court whenever property values or rates decline. This control, however, is stripped from the rights of creditors by allowing the modified home mortgages to be paid over 30 years. H.R. 3609 thereby would ensure more borrowers will seek Chapter 13 bankruptcy for home loans.

In addition to the restriction mentioned above, vacation homes and investment properties seldom get to the point of cram down because there is generally little reason to cram down these loans. A vacation home clearly is not necessary to provide a roof over the borrower's head and with no equity, and little or no income, is a burden on the estate. Likewise, an investor property that has no equity and a negative cash flow is not necessary for reorganization and is a burden on the estate.[3] Thus, cram down of these types of loans is seldom attempted. Instead, the lender obtains termination of the automatic stay and the property is foreclosed without stripping down the lien. Conversely, a principal residence *is essential* to the reorganization of the borrower and thus if H.R. 3609 were enacted, courts would not release the assets from the stay and judges would be required to impose strip down of the lien. In effect, H.R. 3609 would treat home mortgage debt far worse than other secured debts in bankruptcy.

By stripping down secured debt, H.R. 3609 also would make more funds available in the repayment plan for credit cards and other unsecured debts. This is contrary to the basic legal premise of secured debt. Bankruptcy is generally a zero sum proposition. If funds are deducted from one set of debts – the priority debts, such as a home mortgage – it makes more funds available for non-priority and unsecured debts. While it may not be this Committee's intent to shift the bankruptcy process to the advantage of credit card and other unsecured lenders, this would be one of the impacts.

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[2] 11 USC 1322(d)(2007). See also In re Enewally, 368 F.3d 1165 (9^{th} Cir., 2004).

[3] Investment properties with no equity but with a positive cash flow are still subject to repayment during the 3/5 year term of the plan and thus seldom get crammed down.

Because H.R. 3609 also removes the credit counseling requirement when the debtor has received notice of possible foreclosure, the bill would remove the final control against unfettered bankruptcy filings. Congress enacted the pre-filing counseling requirement to assure that debtors in financial difficulty had the benefit of two independent sources of information – approved non-profit counselors and bankruptcy attorneys. Credit counselors are well-versed in housing assistance to help a borrower save his home without filing bankruptcy.

There is no doubt the impact of the modification provision combined with elimination of all creditor protections would result in increased Chapter 13 filings. The considerable incentive of financial gain to the borrower would ensure cram downs on home loans would skyrocket. Servicers, portfolio lenders and bondholders would suffer significant losses. New creditworthy borrowers would have to pay for the value of these "takings." Financially responsible borrowers in the future would pay for the risky behavior and speculative decisions made by existing borrowers. Lenders would have a fiduciary duty to offset losses created by this bill through higher interest rates, points and fees on new loans. Anticipated losses from cram downs could trigger additional lay-offs in the mortgage industry, including lay-offs at mortgage servicers. The legislation would result in a further constriction of mortgage credit. These would not be welcome developments as most companies have tripled or quadrupled staffing to process loss mitigation requests and handle delinquent loans.

C. Cram Downs Voids Significant Types of Credit Enhancements

Proponents of bankruptcy reform argue creditors will take the same losses if the loan is stripped down to the fair market value as they would if the loan is foreclosed. This is a myth, as it fails to recognize certain insurance contracts would be voided for the amount of the cram down.

Specifically, servicers lose their FHA insurance and VA guarantee claims for the amount of any lien strip down. The servicer would have to advance the amount stripped down to Ginnie Mae security holders and absorb the principal loss. This is a substantial shift in liability that servicers certainly did not contemplate when they agreed to service Ginnie Mae securities. As stated previously, servicers rarely take principal losses today. The severity of losses to which servicers would now be exposed would be comparable to what FHA and VA lose with each foreclosure – more than $30,000 per property. Yet, if those loans went to foreclosure sale, FHA insurance and VA guarantees would protect the servicer against principal loss.

VA and FHA loans are not insulated from the havoc H.R. 3609 would wreak. In fact, the Chabot Compromise's definition of subprime as a loan with a three point spread over Treasury securities of comparable maturity measured at the time of application ensures a significant number of government loans (and prime loans) would be eligible for lien stripping.

The risk of uninsured losses and repurchase risk created by H.R. 3609 would cause existing servicing portfolios to decline in value, requiring accounting write downs of servicing assets. The velocity at which loans would enter bankruptcy could cause capital and liquidity problems for servicers. This disruption could also cause significant problems with voluntary mortgage workouts as bankruptcy cram downs would consume the servicer's financial and personnel resources. The stated objective of encouraging more voluntary workouts through H.R. 3609 would simply not materialize because (1) the reward in bankruptcy is far more lucrative than what servicers could offer and (2) servicers may have to cut costs to offset losses by eliminating critical jobs.

When these government programs were created, there was no risk of cram down on home mortgages. As a result, authorizing statutes and regulations of the government programs fail to deal appropriately with the risk that would be created by H.R. 3609. Statutes were developed to deal with foreclosures, not bankruptcy modifications and strip downs. FHA and VA are not permitted *by statute* to pay an insurance claim or guarantee for the strip down amount. [4] It was simply not contemplated. An additional act of Congress would be required to restore these credit enhancements.

At a time when the public policy process is moving toward an increased reliance on the FHA and VA to serve the low income and first time homebuyers, H.R. 3609 would disadvantage government lending and drive lenders away from it.

D. Impact of Cram Downs on Investors and the MBS Market

Securitization increases homeownership. Today, banks and other lenders resell mortgage debt to other investors, or "securitize" it. This frees up capital and allows banks and mortgage companies to invest more into local economies and makes home mortgage credit more widely available. As a result, homeownership has risen significantly since the mid-1990s. The share of Americans who owned homes rose from 64 percent in 1994 to 69 percent by 2005. This is the highest increase in homeownership since the surge that followed World War II.

Securitization of mortgages is based on the underlying value of those mortgage contracts. Granting bankruptcy judges the authority to retroactively modify a mortgage in Chapter 13 proceedings would have a materially adverse impact on the mortgage contract. The resulting uncertainty would mean securitizers or

[4] 12 USC 1710a (2007). FHA can only pay a claim when it receives title to the property, the mortgage is foreclosed, the loan gets assigned, there is a pre-foreclosure sale or there is a loss mitigation partial claim. A partial claim is a specialized loss mitigation tool, which allows arrearages to be subordinated into a junior lien held by HUD. VA is only allowed to pay the unpaid principal balance, plus accrued interest and applicable charges. 38 USC 3832 (2007).

investors could not assess prices or calculate the risk of how many mortgages could be modified. If, with a stroke of a pen, the US government could eliminate the entire secured nature of these investments whenever there is a cyclical down turn in the real estate market, why would investors return the our mortgage markets? They would simply take their money to other more secure and predictable investments. Existing MBS values would also decline as investors dump MBS collateralized by subprime and at-risk assets and as credit rating agencies further downgrade securities.

Investors such as Fannie Mae and Freddie Mac also would be required to purchase the covered loans out of the MBS pools if the loans are modified and absorb the principal losses.

E. Lenders Will be Forced to Absorb the Risk of Properties Damaged by Natural Disasters or Borrower Misconduct

Another significant concern created by H.R. 3609 would be the windfall borrowers would obtain when the property is either 1) damaged by the borrower or 2) damaged by natural disasters such as Hurricanes Katrina and Rita or the recent wildfires of southern California.

Borrowers in default often fail to properly maintain their property, and sometimes intentionally damage their property. In some cases, borrowers attempt significant renovations but fail to complete them, leaving the collateral significantly devalued. We do not believe these debtors should be rewarded through loan stripping, but H.R. 3609 would do just that if passed.

Likewise, we do not think borrowers should be able to wipe out the security interests of creditors when their properties are destroyed by natural disasters, but H.R. 3609 could do just that. A recent relevant example is the damage to properties from Hurricanes Katrina and Rita. As you may know, lenders have offered borrowers who were impacted by the hurricanes over two years of forbearance and/or have also modified their mortgages. Some properties have zero or negative values. Now that insurance and Community Development Block Grant (CDBG) money is flowing to homeowners to rebuild these properties, this legislation would render a devastating blow to investors and servicers: the ability for borrowers to wipe out *all or significant portions* of the debt in Chapter 13 bankruptcy.

The impact of lien stripping on insurance proceeds and grant funds as secured assets is also brought into question. Based on cases associated with other secured debts, it appears creditors may lose their secured interests in hazard insurance proceeds for the amount of the cram down, with possibly no recourse to recover the value of the original debt. H.R. 3609 would place lenders, servicers and investors in an inappropriate role of property insurers of last resort and/or guarantors of property values. Lenders and servicers would not have priced for the risk at origination, and would require cross-subsidization from new originations to avoid massive losses. That cross-subsidization would result in higher costs for new loans.

Myth: Consumers' Only Benefit Will Be Foreclosure Avoidance
Fact: H.R. 3609 Gives Enormous Windfalls to Borrowers

What is probably one of the most inequitable results of H.R. 3609 is the fact that debtors in depressed real estate markets or with damaged or destroyed properties would reap a windfall at the expense of borrowers who honor their debts, as well as servicers and investors. This windfall would occur if the borrower is permitted to reduce the debt to the depressed value of the property, retain the property and realize future appreciation in value when market conditions improve (or repairs get made with insurance and government aid), while having no obligation to pay the lender the full contractually agreed upon debt. Executing a strip down based on a snapshot of value ensures borrowers will make significant profits when the property appreciates later in time. The case in point is illustrated by <u>In re: Enewally</u> 368 F.3d 1165 (9th Cir., 2004).[5] Despite the current market turndown, over the last 30 years home prices nationally have risen six percent per year on average.[6]

The unfair result H.R. 3609 would create does not occur today in Chapter 7 or when the borrower is allowed to foreclose on the property. The creditor in either case would have the right to acquire the property by bidding its claim. The creditor could then, if it chose, hold the property until market conditions improved (and retain full mortgage insurance benefits and security interests in hazard insurance and grant proceeds in the case of damaged property), thereby reducing its losses. Furthermore, with foreclosures, the servicer could in most cases seek a deficiency judgment for the difference between the value of the property and the contractual obligation. No such remedies are permitted in H.R. 3609.

Myth: H.R. 3609 Is Needed Because the Mortgage Industry Is Not Doing Enough to Help Borrowers in Need
Fact: Industry is Engaged in Historic Efforts to Assist Distressed Borrowers

Recently, MBA released an empirical report on how servicers helped borrowers in the third quarter of 2007. As indicated earlier, this was before the HOPE NOW initiative got off the ground, so it gives a good sense of servicers' traditional

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[5] At the time of the bankruptcy court's ruling in 2001, the debtor's property had declined in value to $210,000. The mortgage debt was approximately $245,000 and the borrowers sought cram down. However by the time the United States Supreme Court rejected the Writ of Certiorari three years later, that same property was worth $600,000. Had the debtors' cram down not been overturned on appeal, the debtors would have received a significant windfall.
[6] OFHEO House Price Index.

ability to help, while also setting a floor from which the industry could be judged moving forward. The report is included in the testimony, but several important facts should be highlighted.

During the third quarter of last year, mortgage servicers helped about 183,000 borrowers through repayment plans. They modified the rates or terms on about 54,000 more loans, 3,000 of which were subprime ARM loans, 15,000 subprime fixed rate loans, 4,000 prime ARM loans and 21,000 prime fixed-rate loans. As you can see from these numbers, the industry helped over 230,000 borrowers.

The MBA paper also discussed something known in our industry as the "Moody's One Percent Number." In September 2007, Moody's released a study suggesting the mortgage industry had assisted only one percent of the people who needed help. A later report then increased the number to 3.5 percent. Unfortunately, these numbers were not put into the proper context and represent a poor picture of how many people have been helped. In fact, the Moody's report that indicated loan modifications had increased to 3.5 percent, clearly noted the actual percentage of borrowers who received some type of ***workout*** was 24 percent.

The problem with this type of analysis is the math was off in two places. In order to come up with a percentage, a researcher uses simple high school level division, with a numerator and a denominator. The Moody's report limits the numerator to loan modifications and excludes all other types of assistance offered to borrowers. As discussed earlier, borrower assistance can come in many different forms. This is not the kind of process that produces a single solution for every consumer. The denominator Moody's used was the complete universe of subprime ARMs whose rates reset in a particular period. In the third quarter of 2007, according to MBA's National Delinquency Survey, over 80% of subprime ARM borrowers were paying on time. Certainly Moody's was not advocating that mortgage servicers modify the loans of people who are paying on time and who had not contacted the servicer for assistance?

A more appropriate measure is to look at the number of people helped relative to the number who become seriously delinquent or request help. It makes no sense to compare the smallest possible number of people who get help (those who receive formal loan modifications) against the largest possible number of borrowers (the total number of resetting subprime ARMs).

Members of this Committee have discussed their goal of keeping people in their homes. The Mortgage Bankers Association absolutely shares that goal. No one wants a family to lose its home and MBA's members are trying their best to help. Servicers are providing unprecedented levels of loss mitigation to eligible borrowers in distress. These alternatives to foreclosure include forbearance and repayment plans, modifications, partial claims, short sales and deed in lieu of foreclosure.

The single largest barrier to helping consumers is the low contact rate servicers have with borrowers. Historically, 50 percent of borrowers who reached foreclosure had no contact with the servicer despite multiple efforts on the servicer's part to reach out. Contact volume is still low and borrowers often simply don't know where to turn for reliable advice and assistance. Servicers have been working diligently to ensure all borrowers know about alternatives to foreclosure and to coordinate with housing counselors if borrowers are uncomfortable talking to their servicers. To help provide a coordinated and centralized approach to foreclosure prevention, the industry, with the assistance of the Department of Treasury and Department of Housing and Urban Development launched HOPE NOW.[7] While Faith Schwartz, Executive Director of HOPE NOW, will provide greater detail on the accomplishments of the industry, it is important to highlight HOPE NOW servicers have mailed approximately 500,000 letters to no-contact delinquent borrowers alerting them of the servicer's loss mitigation telephone number and the toll free HOPE Hotline. In addition, HOPE NOW servicers are centralizing their points of contact for expedited service to counselors and are providing counselors with new technology to expedite loss mitigation solutions.

Myth: Bankruptcy is the Preferable Way to Help Consumers
Fact: Bankruptcy is a Long, Difficult and Burdensome Process with Severe Long-Term Negative Consequences for Consumers

The proponents of bankruptcy reform fail to acknowledge the very real and severe consequences for consumers who declare bankruptcy. A bankruptcy stays on a consumers' credit report for 10 years, making it difficult to acquire future credit, especially in the tighter credit environment. Bankruptcy makes it more difficult for borrowers to get credit cards, buy a home, car or hazard insurance and in some cases, obtain employment. Bankruptcy costs consumers about $3,000 in attorney and court fees. Two-thirds of bankruptcy repayment plans fail. Moreover, bankruptcy repayment plans do not take into account new expenses that an individual incurs, such as unanticipated health related costs or emergencies. Attached to the testimony is a document produced by Professor Lynn M. LoPucki detailing the bankruptcy process (also available at http://www.bankruptcyvisuals.com/viewcharts.html). It is inconceivable Congress would rather push people into this process rather than focus on other more effective and less burdensome ways to help consumers.

Myth: H.R. 3609 Will Put Second Lien Holders in No Worse Position Than They Are Today
Fact: The Second Lien Market Will Be Badly Hurt from this Legislation

The second mortgage market has been particularly hard hit by current declining real estate values. Many borrowers are not paying their second mortgages when the fair market value of their property declines below the principal balance of the

[7] http://www.hopenow.com/

second loan. The second lien holder is left with no other option, but to allow the delinquency to continue, but retain the lien. They are not foreclosing on the second mortgages. These delinquent borrowers are not necessarily insolvent. Eventually home values will rise and these borrowers will begin repaying their second liens. H.R. 3609 would take away the lender's right to retain the lien and seek repayment at a later date. H.R. 3609 would wipe out existing second lien holders that are deemed subprime.

These second liens serve as credit enhancements for many first mortgages in the subprime market and thus are not and should not be extinguished indiscriminately. Proponents claim lenders are no worse off in bankruptcy than in foreclosure. This is a myth. This facile analysis fails to recognize many lenders, especially second lien lenders, are not seeking foreclosure, and are thus preserving their assets. H.R. 3609 would strip lien holders of this crucial right, effectively taking the asset from them.

Myth: Congress Has Not Done Enough to Address the Subprime Crisis
Fact: Congress Can Take Great Pride in Its Response to the Crisis

Members of the House can take considerable pride in the steps taken to address problems in the mortgage market. The House passed legislation modernizing the Federal Housing Administration (FHA), giving it a greater ability to help troubled borrowers refinance their loans. The House passed legislation that would exclude discharged debt on principal residences from gross income for tax purposes, thereby saving borrowers already in trouble from higher tax bills and encouraging work outs. The House passed meaningful housing government sponsored enterprise (GSE) reform and passed legislation establishing an affordable housing trust fund to ensure more high quality housing is available for more low- and moderate-income families.

Moreover, the House passed H.R. 3915 that would create a new legal regime for the mortgage market. This is a very serious piece of legislation. The mortgage industry believes it should be significantly improved. As this activity shows, the answer to this problem lies in improving the statutes governing lending, not in amending the bankruptcy code.

In addition to Congressional actions, FHA recently announced FHASecure,[8] which allows borrowers the opportunity to refinance into FHA insured loans. What is remarkable about this program is that it would allow a borrower who is six months delinquent on an ARM to refinance into an FHA loan, despite his or her delinquency, provided the borrower had a good payment history prior to the ARM rate reset and can afford the new payments. The program also allows borrowers who are upside down on their mortgages (i.e., owe more than their property is worth) to refinance a portion of their loan into non-FHA insured subordinate liens. In the past, combined loan-to-value requirements prohibited

[8] http://www.fha.gov/about/fhasfact.cfm

such activity. Unfortunately, it is unclear whether the threat of H.R. 3609 would discourage these subordinate loans from being originated, thus depriving borrowers of useful assistance.

While Congress has made strides in assisting borrowers in distress, H.R. 3609 would go too far. It encourages damaging behavior that would only serve to increase the cost of credit to financially responsible borrowers in the future and would place at risk the solvency of mortgage servicers and lenders, while also reducing the value and yield on certain securities.   It would repudiate existing contracts, void credit enhancements, rights to certain insurance claims, trigger mandatory buyback options and impose a home price guaranty on existing mortgages. For proponents to argue these changes would not have a significant affect on lenders, servicers and bondholders is either dangerously naïve or simply disingenuous.

Conclusion

MBA opposes H.R. 3609 because of the harm it would cause to the mortgage market and borrowers who seek home mortgages. While well-intentioned, H.R. 3609 would increase rates significantly, dry up investor interest in mortgage-backed securities and impose significant losses on the mortgage industry and bondholders. Credit enhancements that protect lenders and investors from loss in the event of foreclosure would be void for the amount of the lien strip. Noteholders' interest in insurance claims would be at risk. With investor appetite for U.S. mortgages waning, it is ill-advised to pass legislation that would further disrupt the mortgage market. We urge Members of the House to look deeper into the implications of H.R. 3609. We are convinced that upon further detailed analysis you will agree that further action on this legislation is ill-advised.

Thank you for this opportunity to share our concerns with the Subcommittee.